

Bond Market Insight

FX-denominated bills support budget financing

Comment on government bond placement

Yesterday, UAH6bn (US\$215m) was borrowed for the budget, of which US\$112m was FX-denominated paper. A large amount of UAH-denominated bills were also sold.

About US\$112m, or more than UAH3bn, will be received today in budget accounts from USD-denominated paper with 13-month maturity. This issue, the same as the FX-denominated bills, was offered the first time in September. Demand was concentrated; most of the bids came in at 3.5%, the highest was 4%. The Ministry rejected two bids. Both the number of bids and amount of demand were larger. There were 30 bids with 28 bids accepted, or six bids more than in August. Total demand was UAH111bn or almost four times more than three weeks ago.

Table 1. Details of domestic government bonds placed at the auction (UAHbn)

ISIN	Coupon rate (%)	Payment frequency	Maturity	Qty of bonds sold	Price (UAH)	Proceeds ² (UAHm)	Volume ² (UAHm)	YTM ³ (%)	Out-standing (m) ⁴
UA4000211957	0.00	@Mty	28-Apr-21	2,095,470	954.21	1,999.52	2,095.47	7.82	2,095.47
UA4000204572	16.06	SA	3-Aug-22	803,573	1,112.30	893.82	803.57	10.73	8,993.64
Total UAH				2,899,043		2,893.33	2,899.04		11,089.11
UA4000211502	3.50	SA	21-Oct-21	110,304	1,014.11	3,138.91	3,095.24	3.53	3,921.10
Total USD				110,304		3,138.91	3,095.24		3,921.10

Note: [1] payment frequency abbreviations: M - monthly, Qtly - quarterly, SA - semi-annually, @Mty - at maturity date; [2] proceeds and volumes for the USD-denominated bonds are calculated based on the previous day's exchange rate 28.06/USD, 30.23/EUR; [3] yields on coupon-bearing bonds are effective yields to maturity. Sources: Ministry of Finance of Ukraine, Bloomberg, ICU.

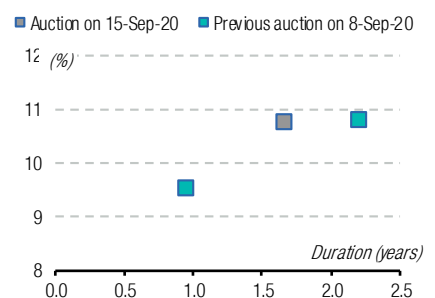
There were fewer participants for the auction of UAH-denominated bills. Most of the interest was for the two-year paper, where the MoF received seven bids instead four as it got for the seven-month paper. However, there was larger demand at par value for the seven-month bills than for the two-year instrument.

Demand for seven-month paper came to UAH2.5bn (US\$0.9bn) where UAH410m (US\$15m) had a rate higher than what was accepted at a previous similar offering, which was rejected. Therefore, for this maturity both the cut-off and weighted-average rate remained unchanged at 7.82%.

The Ministry decided to increase rates for the two-year paper, although less aggressively than last week. Demand mostly ranged between 10.25% and 10.5%, while the highest rate was 11%. Therefore, one bid that amounted to UAH100m was rejected. The budget received almost UAH900m with a cut-off rate 10.5% or

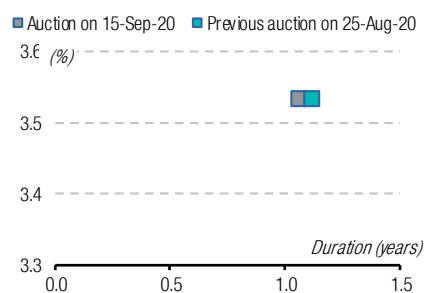
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UAH-denominated domestic gov't bonds: yield curve in past two auctions



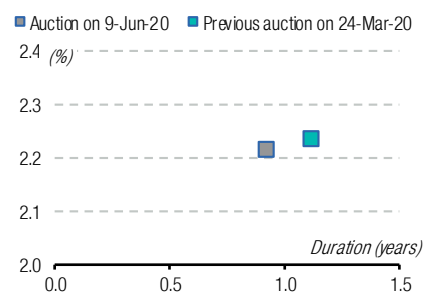
Source: Ministry of Finance of Ukraine, ICU.

USD-denominated domestic gov't bonds: yield curve in past two auctions



Source: Ministry of Finance of Ukraine, ICU.

EUR-denominated domestic gov't bonds: yield curve in past two auctions



Source: Ministry of Finance of Ukraine, ICU.

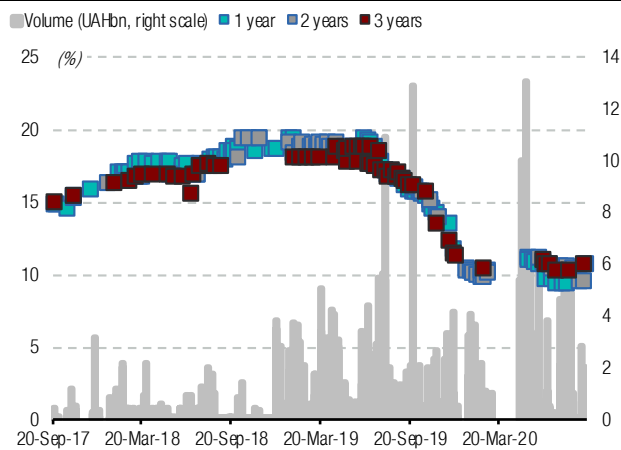
25bp higher than at previous auctions, while the weighted-average rate was up 29bp to 10.43%.

We note that the Ministry continues to use FX-denominated paper to finance budget needs. However, for UAH-denominated bills, the Ministry is flexible and adjusts to market sentiment. We'll see how long this flexibility lasts, as any rate increase makes debt service more expensive for the state budget, and can push bidders to further increase in rates at the primary auction. This could result in rejecting all demand if it becomes too expensive for the MoF.

Appendix: Yields-to-maturity, repayments

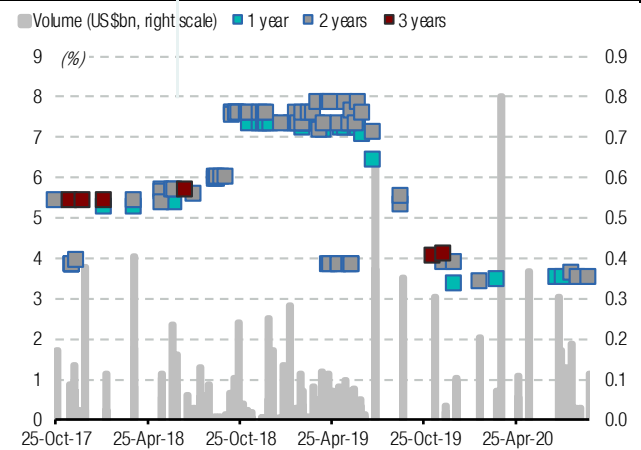
Chart 1. Three-year history of domestic government bond placements at primary market: proceeds (in billions) and yields-to-maturity (%)

UAH-denominated domestic government bonds



Source: Ministry of Finance of Ukraine, ICU.

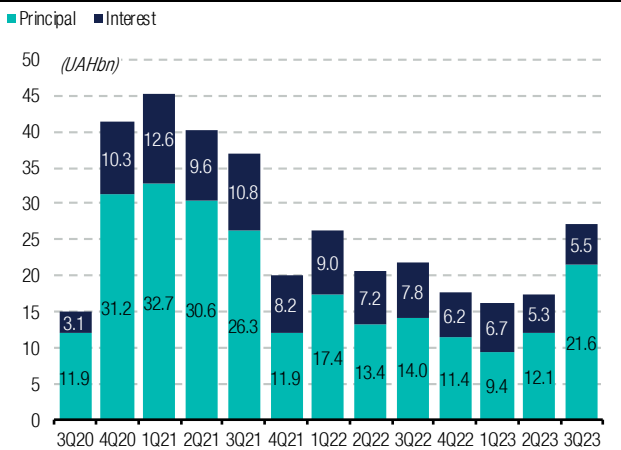
USD-denominated domestic government bonds



Source: Ministry of Finance of Ukraine, ICU.

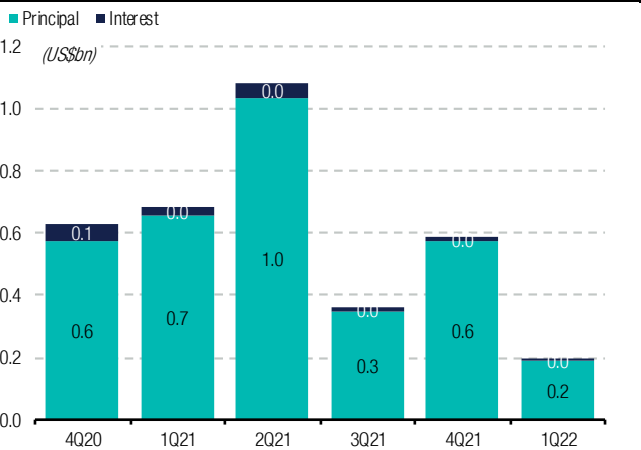
Chart 2. Future repayments on domestic government bonds (in billions of currency)

UAH-denominated domestic government bonds



Source: Ministry of Finance of Ukraine, ICU.

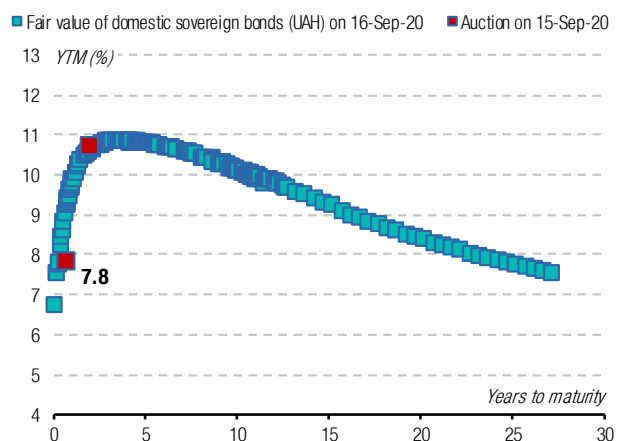
USD-denominated domestic government bonds



Source: Ministry of Finance of Ukraine, ICU.

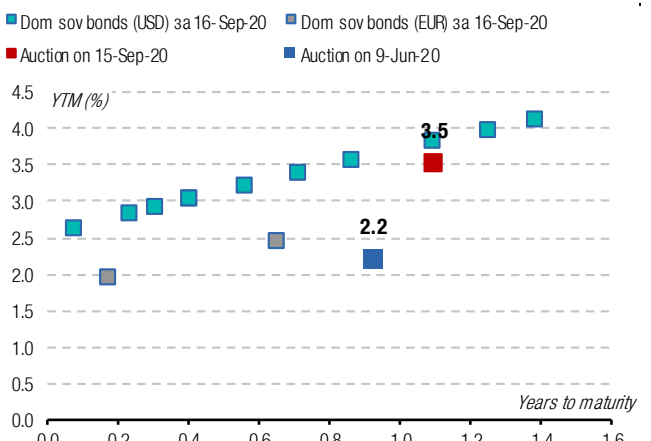
Chart 3. Fair value of domestic government bonds as calculated by NBU versus placements via primary market auctions

UAH-denominated domestic government bonds



Source: National Bank of Ukraine, Ministry of Finance of Ukraine, ICU.

USD- and EUR-denominated domestic government bonds



Source: National Bank of Ukraine, Ministry of Finance of Ukraine, ICU.

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11th floor, LEONARDO Business Centre
19-21 Bogdan Khmelnytsky Street
Kyiv, 01030 Ukraine
Phone/Fax +38 044 3777040

WEB www.icu.ua



RESEARCH

Sergiy Nikolaychuk

Head of macro research
sergiy.nikolaychuk@icu.ua

Taras Kotovych

Senior financial analyst (Sovereign debt)
taras.kotovych@icu.ua

Dmitriy Dyachenko

Junior financial analyst
dmitriy.dyachenko@icu.ua

Alexander Martynenko

Head of corporate research
alexander.martynenko@icu.ua

Mykhaylo Demkiv

Financial analyst (Banks)
mykhaylo.demkiv@icu.ua

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